

**Results of Year-End
Inventory Test Counts
June 30, 2017
AR 18 - 01**



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A handwritten signature in cursive script, reading "Deborah Welch", is written over a horizontal line.

Deborah Welch
Chief Internal Auditor

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September 18, 2017

AR 18 - 01

EXECUTIVE SUMMARY

What We Reviewed

As required by the City Charter, an independent audit of the City's financial records is conducted each year. The audit includes various tests of City accounts, records and financial transactions as considered necessary to formulate an opinion as to whether the City's financial statements fairly represent the financial position of the City. On June 30, 2017, inventories of materials and supplies held by City departments was valued at **\$2,669,725.71**.

City departments that stockpile materials and supplies with a value of more than \$5,000 are required to perform a year-end inventory count and submit the inventory report to the Accounting Division. OIA's performed a year-end test count of City materials and supplies inventories for the following City departments: Fleet Services Division (General Services); the Public Works Division (Transportation and Environmental Services - TES); and, the Corporal Charles W. Hill Law Enforcement Firearms Training Facility (Police Department Range). The value of the three (3) inventories selected for test count by was **\$1,005,618.85**, or **38%** of the inventory total reported for June 30, 2017.

OIA's test count of the three (3) departmental inventories was directed at determining if the inventory existed; if the inventory value was reported accurately to the Accounting Division; and, if the selected departments used a perpetual inventory system to manage their material and supplies inventory.

What We Found

All three (3) departments performed a year-end inventory count and reported the inventory value to the Accounting Division as required. No material exceptions were found during OIA's test counts of the three (3) department inventories. The Fleet Services Division and the Police Department Range use a perpetual inventory system that tracks receipt and disbursement of inventory items. TES Administration is evaluating a warehouse management system and will deploy the warehouse management system department-wide when funds are available.

What We Recommended

The three (3) departments performed a year-end inventory count, with results reported to the Accounting Division as required. We believe that the year-end inventory value for the three (3) departments is fairly stated in the City's financial records. In addition, two (2) of the three (3) departments have implemented an inventory tracking process; and the third department is evaluating a warehouse management system. Accordingly, no recommendations were made.

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Background

As required by the City Charter, an independent audit of the City's financial records is conducted each year. The audit includes various tests of City accounts, records and financial transactions as considered necessary to formulate an opinion as to whether the City's financial statements fairly represent the financial position of the City.

Administrative Regulation 4-4 *Inventory of Supplies and Materials* provides the guidelines for the stockpiling of materials and supplies whose total value exceeds \$5,000. The regulation requires departments to maintain a perpetual inventory system; perform a physical inventory count at year-end; and, report the results of the year-end inventory count to the Accounting Division. In addition, departments are also responsible for the physical security and record keeping functions of receiving, storing, and issuing materials and supplies to support departmental needs. On June 30, 2017, City departments held materials and supplies valued at **\$2,669,725.71**.

Purpose, Scope and Methodology

Purpose

OIA's workplan included test counts of inventories maintained by City departments and was directed at determining if the inventory existed; if the year-end inventory value was reported accurately to the Accounting Division; and, if the selected departments used a perpetual inventory system to manage their material and supplies inventory.

Scope and Methodology

OIA staff selected the inventories maintained by the Fleet Services Division (General Services); Public Works Division (Transportation and Environmental Services); and, the Corporal Charles W. Hill Law Enforcement Firearms Training Facility (Police Department Range) for the test count. Prior to the test count, OIA staff interviewed the Supervisors responsible for taking the year-end inventory count. To assure that all inventory items were reflected on the departmental year-end inventory report, OIA staff selected items from the year-end inventory report and traced them to the physical item. In addition, OIA staff randomly selected items during the inventory test count and tracked the items to the year-end inventory report.

Our review was limited to a test count of inventories held by the three (3) City departments. Accordingly, we have no opinion on overall compliance with policies, procedures, or internal controls in other areas of the departments visited.

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Findings and Recommendations

We found that the three (3) departments performed a year-end inventory count and submitted their year-end inventory reports to the Accounting Division as required by the Administrative Regulation. During our test counts, we found that two (2) of the three (3) departmental year-end inventory reports contained exceptions that either overstated or understated the value of their departmental inventory. However, the amounts were immaterial to the total value of the department inventory.

In addition, we found that two (2) departments use a perpetual inventory system to track inventory; and one (1) department is evaluating a warehouse management system which will be implemented department-wide, once funding is available.

1. Results of Inventory Year-End Test Counts

City departments maintain supplies and material inventories to accomplish their stated missions. The inventories for the three (3) departments selected include vehicle maintenance parts (tires, oil, batteries, etc.); chemical stockpiles and mission critical inventory items (road salt, sand, calcium chloride, manhole covers, fire hydrants, etc.); and, training materials (ammunition and targets.)

(a) Fleet Services Division (General Services)

As required by the Administrative Regulation, the Fleet Services Division conducted a year-end inventory count and submitted the year-end inventory report with a value of **\$262,603.93** to the Accounting Division. For the test count, OIA staff selected a total of **56** items from the year-end inventory report. The dollar value of our test count was **\$25,682.21**, or almost **10%** of the total dollar value of the Fleet Services Division's inventory at June 30, 2017.

Three (3) exceptions were noted during the test count. The total amount of the exceptions resulted in an overstatement of Fleet Services' inventory by **\$905.71**. Fleet Services staff adjusted the inventory totals in the FASTER system, but failed to adjust the items on the year-end inventory report provided to the Accounting Division. The overstatement did not materially effect the value of Fleet Services inventory for FY 2017. Accordingly, no recommendations were made.

(b) Public Works Division (Transportation and Environmental Services)

As required by the Administrative Regulation, the Public Works Division conducted a year-end inventory count and submitted the inventory report with a value of **\$467,721.23** to the Accounting Division. For the test count, OIA staff selected a total of **33** items from the year-end inventory report. The dollar value of our test count samples was **\$45,772.56**, or almost **10%** of the total dollar value of the Public Works Division's inventory at June 30, 2017.

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Five (5) exceptions were noted during the test count. The total amount of the exceptions resulted in an understatement of the Public Works Division' year-end inventory by **\$134.48**. Public Works Division staff failed to adjust the items on the year-end inventory submitted to the Accounting Division. The understatement did not materially effect the Public Works Division's inventory value for FY 2017. Accordingly, no recommendations were made.

(c) Police Department Range

Prior to June 30, 2017, the Range did not perform a year-end inventory count or report the value of inventory maintained to the Accounting Division. The inventory items maintained at the Range include nine (9) types of ammunition (pistol, rifle and shotgun) and targets. OIA staff met with the Range Manager and discussed the requirement to perform a year-end count and to report the value of the inventory to the Accounting Division. Range staff conducted a year-end inventory count for FY 2017 and submitted the year-end inventory report with a value of **\$275,293.69** to the Accounting Division.

Since this was the first year-end count conducted by the Police Department Range, OIA staff counted the nine (9) types of ammunition maintained at the Range. The dollar value of the test count was **\$172,006.26**, or **62%** of the total dollar value of the Police Department Ranges inventory on hand at June 30, 2017.

During discussions with the Range Manager, we were informed that 400 cases of .40-caliber practice ammunition (valued at **\$99,996**) purchased from a City vendor on March 15, 2015, is being held offsite by the vendor. Due to the limited storage at the Range and the pending renovation to the Police Department Range, the vendor agreed to maintain custody of the ammunition. The value of the ammunition stored off-site has been included with the year-end inventory.

The Range Manager, who was hired on July 6, 2016, is now aware of the requirement to perform a year-end inventory count and will include the count as part of the year-end activities in June 2018. In addition, the Range Manager will monitor the situation with the .40-caliber practice ammunition and will take physical custody of the ammunition once the renovation of the Range is complete.

OIA staff will follow-up with the Range Manager in June 2018, to ensure that a year-end inventory is performed and to check the status of the renovation and the ammunition stored off-site.

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2. Utilization of Perpetual Inventory Systems

Administrative Regulation 4-4 *Inventory of Supplies and Materials* mandates the use of a perpetual inventory system to track inventory usage in City departments. A perpetual inventory system is an effective inventory tool that tracks, in real-time, the receipt and disbursements of inventory items. A perpetual inventory system has the following benefits: program generated re-order notifications; off-the-shelf items can be ordered on an as-needed basis; inventory items that are no longer used can be identified and removed from the re-order process; unusual inventory shrinkage can be identified quickly; and, the security over inventory items is enhanced. To be effective, a year-end inventory count must be conducted to verify the items on hand.

(a) Fleet Services Division (General Services)

The Fleet Services Division maintains their inventory of vehicle maintenance parts on a perpetual inventory system known as FASTER. This system has been in use for several years. The reports produced from the FASTER system are checked periodically by Fleet Services staff members to ensure an accurate accounting of parts on hand, as well as to identify obsolete and surplus parts. The Fleet Services Division is in compliance with the requirement to use a perpetual inventory system.

(b) Public Works Division (Transportation and Environmental Services)

During our review, we found that the Public Works Division does not use a perpetual inventory system to track their inventory. However, a new warehouse management system is under review by T&ES management. Once funding is available, the warehouse management system will be expanded to all department-wide inventories (Traffic Control Shop and Maintenance Division). Accordingly, no recommendations will be made regarding the lack of a perpetual inventory system in the Public Works Division.

(c) Police Department Range

Staff at the Police Range perform two (2) primary functions. The Police Range is used to train and qualify Alexandria public safety officers (including Sheriff Deputies and Fire Marshals) and a small number of federal and local agencies, with regard to duty pistols, rifles and shotguns. To do so, ammunition (both practice and duty) is maintained on-site. Each public safety officer is provided practice ammunition to use during the training and qualification process. The amount of practice ammunition provided, depends on the officer's department/agency and duty assignment. Once training is complete, the Range Manager issues duty ammunition to the officer. The inventory tracking process created by the Range Manager tracks the ammunition received and issued by type and by certification class.

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Prior to June 30, 2017, the Police Department Range did not utilize a perpetual inventory system. However, Range staff designed an inventory control spreadsheet that tracks both the purchase and use of the nine (9) types of ammunition stocked at the Range. The inventory control spreadsheet tracks the practice rounds fired during the officer qualification sessions and the duty ammunition issued to officers once they have qualified. An attendance spreadsheet tracks the individuals in each qualifying session.

Due to the limited number of items maintained at the Range, the inventory tracking process created by the Range Manager will act as a basic perpetual inventory system tracking the receipt and issuance of the primary inventory item – ammunition. The receipt of inventory can be tracked through the City's financial system and the disbursement can be tracked using the sign-in sheet created for each qualifying class.

No recommendation was made with regard to the inventory tracking process created by the Range Manager. However, OIA staff will follow-up with the Range Manager in June 2018, to ensure that the inventory tracking process is being used.

Conclusion

On June 30, 2017, inventories of materials and supplies held by City departments was valued at **\$2,669,725.71**. The three (3) department inventories selected by OIA were valued at **\$1,005,618.85**, or 38%, of the total reported value of all City inventories for fiscal year 2017. We found no material exceptions during our test counts of the three (3) City inventories. Accordingly, we believe that the value of the assets as reflected in the City's financial statements is fairly stated.

Two (2) of the three (3) departments have an inventory tracking system and the third department is evaluating a warehouse management system. Accordingly, no recommendations were made.

